YMF

v.

KETUA PENGARAH HASIL DALAM NEGERI

SPECIAL COMMISSIONERS OF INCOME TAX
NOOR AZIAN SHAARI
KP RAMACHANDRAN
KAMARUDIN MOHD NOOR
[APPEAL NO: PKCP(R) 55/99]
19 APRIL 2000

REVENUE LAW: *Income tax - Profits from sale of inherited land - Whether taxable under s. 4(a) Income Tax Act 1967 - Whether gains or profits from business - Whether disposal of land in the course of seller's trading activities - Whether joint venture agreement between parties an adventure in the nature of trade*

The appellant inherited a piece of land ('the land') from his late father in 1974. The appellant went into a joint venture agreement with a company called Sunrise Sdn Bhd ('Sunrise') to develop and construct building units on the land but that venture subsequently failed. The appellant then went into a new joint venture agreement with another company called Lot One Development Sdn Bhd ('Lot One') whereby he received 18% of the total saleable units valued at RM22,184,992 for the transfer of the land to the said company. Subsequently, the respondent raised an assessment for the Year of Assessment 1992 on the appellant for a sum of RM7,579,027.74 being income tax on the amount of RM22,184,992.

The appellant appealed to the Special Commissioners of Income Tax against the said assessment. Also that the Year of Assessment should be 1991 and not 1992.

The issues were: (1) whether the profits from the disposal of the land were profits from the disposal in the course of the appellant's trading activity and therefore taxable under s. 4 of the Income Tax Act 1967 ('the Act'); and (2) whether the fact that the appellant had participated in the project for the development of units on the land lent weight to his trading activity.

Held:

[1] The fact that the nature of the asset lends itself to commercial transactions does not, without more, make it a trading activity. The land was inherited and therefore required much more to be classified as trading stock. From the evidence adduced, it was not shown whether the joint venture with

Lot One was a transaction in the appellant carrying on of a trade or the transaction was an adventure or concern in the nature of a trade.

[2] Due to his earlier bitter experience with Sunrise, it was only sheer prudence that the appellant participated in its joint venture with Lot One. To hold that the prudent acts of the appellant amounted to an adventure in the nature of a trade was a fallacy.

[3] The joint venture agreement with Lot One alone, in the absence of other evidence to show any trading activity on the part of the appellant, did not make the venture an adventure within the ambit of s. 2 of the Act. The mere fact that an agreement is entered into or that the subject land is disposed of for a relatively high price does not make the transaction a trade or an adventure in the nature of a trade.

[4] By virtue of para. 23 of the Director-General's Circular No. 2 of 1986, if there is insufficient evidence to show that the joint venture is a transaction in their carrying on of a trade or that the transaction is an adventure in the nature of a trade, the transaction will come within the scope of the Real Property Gains Tax Act 1976. Had the appellant received the RM22,184,992 in cash in exchange for the land, the whole transaction would be chargeable to the Real Property Gains Tax Act 1976.

[5] The appellant had discharged his onus of proving that the said assessment by the respondent was excessive or erroneous. Therefore, the gains from the disposal of the land were not subject to income tax and it followed that the Year of Assessment was irrelevant.

[Appeal by YMF allowed.]

[Editor's note: The appeal by the Ketua Pengarah Hasil Dalam Negeri against the decision of the Special Commissioners of Income Tax vide R2-14-3-2000 has been withdrawn.]

Case(s) referred to:
CIR v. Fraser [1942] SC 493 ***(foll)***
CIR v. Reinhold 34 TC 389 ***(foll)***
Colquhoun v. Brooks [1888] 21 QBD 52 ***(refd)***
DEF v. CIT [1950 – 1985] MSTC 482 ***(refd)***
DEF v. The Comptroller of Income Tax [1961] 27 MLJ 55 ***(refd)***
DGIR v. KEA Sdn Bhd [1990] 1 MSTC 3155 ***(refd)***
DGIR v. TCM [1988] 1 MSTC 3006 ***(refd)***
Fry (HM Inspector of Taxes) v. Burma Corporation Ltd 15 TC 113 ***(refd)***
Hudson's Bay Co Ltd v. Stevens [1905] 5 TC 437 ***(foll)***
I Investment Ltd v. CIR [1979] 1 MLJ 4 ***(refd)***
International Investment Ltd v. Comptroller-General of Inland Revenue [1979] 1 MLJ 4 ***(refd)***

L v. CGIR [1973] 2 MLJ 14 ***(dist)***
Leeming v. Jones (HM Inspector of Taxes) – 15 TC 333 ***(refd)***
LFY Sdn Bhd v. CGIR [1988] 1 MSTC 3059 ***(refd)***
Lionel Simmons Properties Ltd. v. CIR 53 TC 461 ***(refd)***
Lower Perak Co-op Housing Society Bhd v. KPHDN [1994] 2 MSTC 3406 ***(foll)***
Martin v. Lowry (H.M. Inspector of Taxes) 11 TC 297 ***(dist)***
McClelland v. Commissioner of Taxation of Australia 1 WLR [1971] 191 ***(refd)***
Newacres Sdn Bhd v. Sri Alam Sdn Bhd [1991] 3 CLJ 2781 ***(refd)***
NYF Realty Sdn. Bhd. v. Comptroller of Inland Revenue [1974] 1 MLJ 182 ***(refd)***
PS Bhd v. DGIR [1995] 2 MSTC 2292 ***(refd)***
Taylor v. Good (HM Inspector of Taxes) 49 TC 277 ***(refd)***
TCS v. DGIR [1971] 2 MLJ 212 ***(refd)***
The Commissioners of Inland Revenue v. Livingston [1927] 11 TC 538 ***(foll)***
The Commissioner of Inland Revenue v. The Korean Syndicate, Ltd. 12 TC 181 ***(refd)***
Williams (HM Inspector of Taxes) v. The Dunn Trust Ltd 31 TC 481 ***(refd)***

Legislation referred to:
Income Tax Act 1967, s. 4(a)

Other source(s) referred to:
Black's Law Dictionary, 5th edn
Malaysian Taxation, Administrative and Technical Aspects, Veerinderjeet Singh, Longman, 2nd edn
Malaysian Taxation - Principles and Practice, Choong Kwai Fatt, 5th edn, p 168
Whiteman on Income Tax, 3rd edn, p 157
Words and Phrases Legally Defined, London, Butterworths, 1989, 3rd edn

Reported by Usha Thiagarajah

Case Stated By Special Commissioners Of Income Tax For The Opinion Of The High Court Pursuant To Para. 34 Sch. 5 Income Tax Act 1967

At a hearing held in Kuala Lumpur on 24 January 2000, the special commissioners of income tax heard the appeal by YMF (hereinafter referred to as 'the appellant') against a notice of additional assessment dated 8 December 1998 showing RM7,579,027.74 being tax payable for the year of assessment 1992 issued by the director general of inland revenue (hereinafter referred to as 'the respondent') under the Income Tax Act 1967 (hereinafter referred to as 'the Act').

The issues for our determination were whether:

(a) The profits from the sale of a piece of land known as EMR 5103 Lot No. 1, Mukim of Kuala Lumpur (hereinafter referred to as 'the subject land') was gains or profits from a business and taxable under s. 4(a) of the Act; and

(b) The respondent is correct in assessing the income for the year of assessment 1992.

Encik S. Somaskantham and Encik Jayatharan Thamotharam Pillai, tax agents appeared for the appellant. Puan Hazlina binti Hussain, legal officer and Puan Kanaga Devi Shanmugam, assessment officer, both of the inland revenue board appeared for the respondent.

The appellant himself gave evidence.

The respondent did not call any witness.

The following documents were tendered at the hearing:

(i) Issue - A

(ii) Statement of agreed facts - B

(iii) Appellant's bundle of documents - C

(iv) Respondent's bundle of documents - D

(v) Appellant's bundle of authorities - E

(vi) Respondent's bundle of authorities - F

(vii) Appellant's submission - G

(viii) Respondent's submission - H

(ix) Bundle of documents of Dynamak Sdn. Bhd. - Al

As a result of the evidence adduced before us, both oral and documentary, the following facts were admitted or proved:

Facts Admitted

(1) The appellant was a full time employee as a marketing executive with Esso (M) Bhd., till he ceased employment in 1985. He is now fifty-nine years of age.

(2) On 26 September 1974 the appellant inherited land EMR 5103 Lot No. 1 Mukim of Kuala Lumpur measuring an area of 5a 0r 23p or 5.144 acres from the estate of his late father Yong Nam.

(3)(a) On 25 July 1983 the appellant went into a land sale agreement with a company called Sunrise Sdn. Bhd. wherein the subject land was transferred to Sunrise Sdn. Bhd. in return for 20% of the total developed units to be built on the subject land.

(b) The company Sunrise Sdn. Bhd., however did not develop and construct the units thereby failing to fulfill the terms of the agreement. The project did not commence.

(c) Both parties signed another agreement dated 11 July 1990 rescinding the above agreement dated 25 July 1983.

(4) In the light of above the appellant went into a new joint venture agreement with a company, Lot One Development Sdn. Bhd., on 2 August 1990 whereby he is entitled to receive 18% of the total saleable units comprising apartments, penthouses, retail shoplots and car parks in return for the transfer of the subject land to the said company.

(5) In a letter, dated 8 August 1991 Lot One Development Sdn. Bhd. wrote to the appellant detailing the allocation of the apartments and penthouses valued at RM22,184,992.

(6) On 18 August 1994 the firm of Chartered Architects Zainal and Teh forwarded the certificate of completion to the contractors M/s Teknik Cekap Sdn. Bhd., and Lot One Development Sdn. Bhd., the developers of the units.

(7) On 12 September 1994 the developers of the units, that is Lot One Development Sdn. Bhd., made available the keys to the appellant's units.

(8) According to the government valuation report dated 10 April 1996 the subject land was valued at RM1,680,000 as at 15 October 1990.

(9) On 8 December 1998 the respondent raised an assessment for year of assessment 1992 on the appellant for a sum of tax amounting to RM7,579,027.74 representing income tax on RM22,184,992 being the 18% of the units referred to in cl 5.1 of the agreement.

Facts Proved

(1) The appellant inherited the subject land upon the death of his father and the subject land was transferred to him on 26 September 1974.

(2) When the joint-venture with Sunrise Sdn. Bhd. failed, the company agreed to retransfer the subject land to the appellant for two million Ringgit (RM2,000,000). However, Sunrise Sdn. Bhd. later agreed to accept a reduced sum of one million Ringgit (RM1,000,000).

(3) Lot One Development Sdn. Bhd. (hereinafter referred to as "Lot One") paid the one million Ringgit (RM1,000,000) to Sunrise Sdn. Bhd.

(4) On the invitation of Lot One, the appellant attended meetings on 27 August 1991 (p. 27 of D), 11 September 1991 (p. 24 of D), 30 September 1991 (p. 21 of D) and 8 October 1991 (p. 15 of D).

(5) The appellant attended the meetings to protect his interest and also because of his experience as a "marketing man" in Esso (M) Bhd., his former employer to ensure proper construction and sales of the units.

(6) The appellant was not paid any fees or allowance for attending the meetings of or with Lot One.

(7) The appellant received 91 units of the total number of units developed.

(8) The appellant had sold about half of the units he received. The balance of the units are kept for investment purposes. He had submitted Form CKHT 1 for real property gains tax purposes in respect of the units disposed of.

Contentions

By the appellant

(1) The profits from the sale of the subject land should not be subjected to income tax under s. 4(a) of the Act on the grounds that –

(i) The subject land was not purchased but inherited;

(ii) There was no development prior to its disposal;

(iii) It is capital enhancement;

(iv) There was no joint-venture business as there was no participation in profits. The joint-venture agreement was merely an agreement to dispose of land in return for which the appellant was to obtain 18% of the units built;

(v) The sale of the subject land was not an adventure or concern in the nature of trade; and

(vi) It was an isolated transaction; and

(2) If it is held that an act of trade was committed on 2 August 1990, the assessment should be raised for the year of assessment 1991.

By the respondent

(1) The profits from the disposal of the subject land was profit from disposal in the course of the appellant's trading activity and therefore liable to tax under s. 4(a) of the Act; and

(2) The profits received by the appellant should be taxed for the year of assessment 1992 as the income accrued on 8 August 1991.

We were referred to the following authorities:

By the appellant

(i) *Leeming v. Jones* (HM Inspector of Taxes) – 15 TC 333;

(ii) *PS Bhd v. DGIR* [1995] 2 MSTC 2292;

(iii) *McClelland v. Commissioner of Taxation of Australia* 1 WLR [1971] 191;

(iv) *DGIR v. KEA Sdn Bhd* [1990] 1 MSTC 3155;

(v) *DGIR v. TCM* [1988] 1 MSTC 3006;

(vi) *DEF v. CIT* [1950 – 1985] MSTC 482;

(vii) *LFY Sdn Bhd v. CGIR* [1988] 1 MSTC 3059;

(viii) *Lower Perak Co-op Housing Society Bhd v. KPHDN* [1994] 2 MSTC 3406;

(ix) *CIR v. Reinhold* 34 TC 389;

(x) *Taylor v. Good* (H.M. Inspector of Taxes) 49 TC 277;

(xi) *Lionel Simmons Properties Ltd v. CIR* 53 TC 461;

(xii) *TCS v. DGIR* [1971] 2 MLJ 212; and

(xiii) *Williams (HM Inspector of Taxes) v. The Dunn Trust Ltd* 31 TC 481.

By the respondent

(i) Income Tax Act 1967;

(ii) *Words and Phrases Legally Defined*, 3rd edn, London, Butterworths 1989;

(iii) *Malaysian Taxation, Administrative and Technical Aspects*, 2nd edn, Veerinderjeet Singh, Longman;

(iv) *DEF v. The Comptroller of Income Tax* [1961] 27 MLJ 55;

(v) *International Investment Ltd v. Comptroller-General of Inland Revenue* [1979] 1 MLJ 4;

(vi) *Fry (HM Inspector of Taxes) v. Burma Corporation Ltd* 15 TC 113;

(vii) *Leeming v. Jones (HM Inspector of Taxe*s) 15 TC 333;

(viii) *The Commissioner of Inland Revenue v. The Korean Syndicate Ltd* 12 TC 181;

(ix) *Black's Law Dictionary*, 5th edn;

(x) *L v. CGIR* [1973] 2 MLJ 14;

(xi) *Martin v. Lowry (HM Inspector of Taxes)* 11 TC 297;

(xii) *Colquhoun v. Brooks* [1888] 21 QBD 52; and

(xiii) *Newacres Sdn Bhd v. Sri Alam Sdn Bhd* [1991] 3 CLJ 2781.

We, the Special Commissioners of Income Tax took time to consider the case and gave our decision on 31 January 2000 for the following reasons –

For convenience, the relevant parts of the Act are reproduced below –

Section 2 Interpretation

'business' includes profession, vocation and trade and every manufacture, adventure or concern in the nature of trade, but excludes employment;

'partnership' means an association of any kind (including joint adventures, syndicates and cases where a party to the association is itself a partnership) between parties who have agreed to combine any of their rights, powers, property, labour or skill for the purpose of carrying on a business and sharing the profits therefrom, but excludes a Hindu joint family although such a family may be a partner in a partnership;

Section 3

3. Charge of income tax.

Subject to and in accordance with this Act, a tax to be known as income tax shall be charged for each year of assessment upon the income of any person accruing in or derived from Malaysia or received in Malaysia from outside Malaysia.

Section 4

4. Classes of income on which tax is chargeable

Subject to this Act, the income upon which tax is chargeable under this Act is income in respect of –

(a) gains or profits from a business, for whatever period of time carried on;

(b) }

(c) }

(d) } ... (not applicable)

(e) }

(f) }

The appellant inherited the subject land from the estate of his late father. On 26 September 1974, the land was transferred to the appellant.

On 25 July 1983, the appellant went into a land sale agreement with a company called Sunrise Sdn. Bhd. whereby the subject land was transferred to the company to be developed and the appellant was to receive 20% of the total units built.

Sunrise Sdn. Bhd. did not develop the land and failed to fulfill the terms of the agreement. On 11 July 1990, the agreement between Sunrise Sdn. Bhd. and the appellant was rescinded and Sunrise Sdn. Bhd demanded two million ringgit in return for the transfer of the land back to the appellant. Subsequently, the sum of RM2,000,000 was reduced to RM1,000,000.

The appellant then entered into a joint venture agreement with Lot One on 2 August 1990 whereby –

(i) Lot One would pay Sunrise Sdn. Bhd. the one million Ringgit for the transfer of the subject land to Lot One; and

(ii) Lot One shall develop the subject land and the appellant was to receive 18% of the units built valued at RM22,184,992.

The appellant was assessed to tax under s. 4(a) of the Act in respect of the units received valued at RM22,184,992 as gains or profits from a business for the year of assessment 1992.

The appellant now appeals against the said assessment contending that –

(i) the gains is not a business income under s. 4(a) of the Act but a realisation of capital asset; and

(ii) the assessment should be raised for the year of assessment 1991.

In support of his contention, the appellant submitted that –

(1) the subject land was inherited from his late father and that the so called joint venture agreement with Lot One is not a joint venture business agreement but merely an agreement for the disposal of the subject land;

(2) the venture with Lot One was not a partnership;

(3) the badges of trade did not exist and the venture does not fall within the definition of "business" in the form of a trade or an "adventure or concern in the nature of trade";

(4) if it is held that the income is subject to s. 4(a) of the Act, the assessment should be for the year of assessment 1991 in view of the fact that the joint venture agreement was signed on 2 August 1990.

The respondent, on the other hand, in support of his case, submitted as follows –

(1) the disposal of the subject land was in the course of the appellant's trading activities;

(2) the joint venture agreement with Lot One which gives the appellant a relatively high return of RM22,184,992 for the subject land which at the material time was valued only at 1.6 million ringgit is in fact a business venture;

(3) the transaction amounted to an adventure in the nature of trade, and therefore it is business;

(4) since the letter informing the appellant that he would be receiving 91 units valued at RM22,184,992 was dated 8 August 1991, the amount had accrued on that date and as such the income received should be assessed to tax for the year of assessment 1992.

The appellant's arguments in the discharge of his onus of proving that the respondent was erroneous in raising the assessment under the Act are briefly as set out below –

a) The signing of the joint venture agreement does not amount to commencing a joint venture business.

b) The joint venture agreement does not bring the deal between the appellant and Lot One within the ambit of the word "business" and/or "partnership" in s. 2 of the Act.

c) There was no sharing of profits except an exchange of units for the subject land.

d) The appellant by virtue of the agreement is indemnified against all losses, damages and expenses.

e) The four badges of trade as in *Leeming v. Jones (supra)* do not exist in this case.

f) The two cases cited by the respondent, namely –

1. *L v. CGIR* [1973] 2 MLJ 14; and

2. *Martin v. Lowry* 11 TC 297,

do not apply in the case before us.

The respondent raised the assessment under s. 4(a) of the Act on the grounds that the appellant commenced a joint venture business with Lot One on 2 August 1990 and that the profits from the disposal of the subject land was profits from disposal in the course of appellant's trading activity.

The respondent concluded that it was appellant's trading activity for reasons set out below –

a) The words "joint venture" connotes an association of persons for the purposes of, *inter alia*, trading.

b) Joint ventures have fiduciary relations.

c) Lot One shall develop the subject land and the appellant shall receive 18% of the units of each type developed.

d) The building plans are to be discussed and reviewed by the appellant.

e) 18% of the units represents 91 units valued at RM22,184,992 and the amount which accrued to the appellant was relatively high.

f) The appellant had participated in the project as evidenced by the minutes of a meeting held on 5 October 1992 as follows –

> 3.1 To form a project management committee comprising the Landowner, the Architect and a representative from AHB to ensure the smooth and speedy completion of the project. This was agreed to by AHB.
>
> (page 9 of Exhibit D)

(g) The appellant played an active role during several working committee meetings by making suggestions and offering his services in the marketing of the unsold units (pp. 14 to 30 of exh. D).

The respondent further argued that the profit which accrued to the appellant was profits taxable under s. 4(a) of the Act and cited the case of *I. Investment Ltd v. CIR* [1979] 1 MLJ 4 where Viscount Dilhorne said –

> ... a company whose business is, or includes, trading *prima facie* begins to trade as soon as it embarks upon the first transaction of a trading nature. The same would apply to an individual who had set himself up as a trader and declared his intention of trading if the transaction fell within the scope of his trade.

It was the respondent's contention that the badges of trade were present and cited the case of *Leeming v. Jones* 15 TC 333 and argued that the following badges of trade existed in this case –

(i) The existence of an organisation;

(ii) Activities which lead to the maturing of the asset to be sold;

(iii) The existence of special skill opportunities in connection with the article dealt with; and

(iv) The fact that the nature of asset itself should lend itself to commercial transactions.

Finally, the respondent submitted that although the appellant inherited the property, subsequent actions taken by the taxpayer in the disposal of the property tantamount to profits chargeable under s. 4(a) of the Act and cited the following cases as authorities to support this contention –

a. *L v. CGIR* [1973] 2 MLJ 14; and

b. *Martin v. Lowry* 11 TC 297

We deliberated on the facts, the contentions, submissions and the case laws cited and considered the following –

In order to decide whether proceeds from the sale of the subject land amounts to profits liable to tax under s. 4(a) of the Act, it is necessary to determine whether the income are profits of a trade or merely accretions to capital.

In this respect *Whiteman on Income Tax*, 3rd edn, says at p. 157 –

> Where the activities of a taxpayer in relation to the acquisition and sale of property are alleged to constitute the carrying on of a trade, it is necessary to determine, after consideration of all the facts of the case, whether the proceeds of sale are profits of a trade, or merely accretions to capital. In the Final Report of the 1954 Royal Commission six "badges of trade" were listed as being the relevant considerations in deciding whether a transaction of purchase and sale which has given rise to a profit is, or is not, to be treated as a trading transaction.

Therefore, it becomes necessary to look for other factors to determine the dominant intention of the appellant. Sharma J in *NYF Realty Sdn Bhd v. Comptroller of Inland Revenue* [1974] 1 MLJ 182 came up with the following criteria for distinguishing between taxable and non taxable selling profits as being useful in determining whether a transaction amounts to a trading activity –

(1) Subject matter of the transaction

> Property which does not yield income or personal enjoyment to its owner merely by virtue of its ownership, and which is normally the subject of trading and rarely the subject of investments, is more likely to have been acquired for the purpose of resale at a profit than property which does yield such income or enjoyment;

(2) Period of ownership

The fact that property is held for but a short time after its acquisition may tend to indicate that the purpose of acquisition was resale at a profit;

(3) Frequency of transaction

If there had been a number of transactions in the same kind of property it may be presumed that the taxpayer's purpose in purchasing the particular property was its resale at a profit;

(4) Alteration of property to render it more saleable

The fact that material alterations or improvements have been made to property or that its character or quality has been changed so as to render it more merchantable would tend to indicate that the properly was derived from a profit making undertaking or scheme. However, if the property was clearly acquired for other purposes, extensive activities to render it more saleable after it is no longer useful for such original purposes would not cause any selling profit to be taxable;

(5) Methods employed in disposing of property

If special exertion is made to find or attract purchasers such as the opening of an office or advertising extensively, such facts tend to indicate the presence of a profit making undertaking. However, such facts would not of themselves cause the profit to be taxable if the original purpose in acquiring the property was to use it rather than to resell it at a profit;

(6) Circumstances responsible for sale

if sale of property is occasioned by sudden emergency or unanticipated need for funds, such facts will tend to indicate that the property was not acquired for the purpose of resale at a profit and that the sale was not pursuant to a profit making undertaking or scheme.

The fact that the nature of the asset lends itself to commercial transactions does not, without more, make it a trading activity. The subject land here was inherited and therefore requires much more to be classified as trading stock.

In this respect, Lord President Clyde's test in *The Commissioners of Inland Revenue v. Livingston* [1927] 11 TC 538 at p. 542 would seem very appropriate –

> I think the test, which must be used to determine whether a venture such as we are now considering is, or is not, "in the nature of "trade," is whether the operations involved in it are of the same kind, and carried on in the same way, as those which are characteristic of ordinary trading in the line of business in which the venture was made.

Further in *Lower Perak Co-op Housing Society v. Ketua Pengarah Hasil Dalam Negeri* [1994] 2 MSTC 3406, Edgar Joseph Jr, FJ cited with approval the case of *Hudson's Bay Co Ltd v. Stevens* [1905] 5 TC 437 where Farwell, LJ said –

> A land owner may lay out part of his estate with roads and sewers and sell it in lots for building, that he does this as an owner, not as a land speculator ... It would be different if a land owner, an individual, entered into the business of buying and developing and selling land; but the case of the owner, whether of land, or pictures, or jewels, selling his own property, although he may have expended money on them in getting them up for sale, is entirely different; he sells as owner, not as trader.

From the evidence adduced, our search for evidence which can show that the joint venture was a transaction in the appellant carrying on of a trade or the transaction was an adventure or concern in the nature of trade, turned futile.

In *CIR v. Reinhold* 34 TC 389 Lord Russell cited Lord President Normand in the case of *CIR v. Fraser* [1942] SC 493 where it was said –

> .... It is in general more easy to hold that a single transaction entered into by an individual in the line of his own trade (although not part and parcel of his ordinary business) is an adventure in the nature of trade than to hold that a transaction entered into by an individual outside the line of his own trade or occupation is an adventure in the nature of trade.

The bitter experience encountered by the appellant in the joint venture with Sunrise Sdn. Bhd. whereby the joint venture failed, and Sunrise Sdn. Bhd. demanded RM2 million (finally settled for RM1 million) from the appellant for the return of the subject land coupled with a seven year unfruitful delay, it is only sheer prudence that the appellant without making the same 'mistake' this time around, attended the meetings with Lot One, made constructive suggestions and offered to help market the units. To hold all these prudent acts of the appellant against him to say that they amounted to an adventure in the nature of trade is a fallacy.

Further, the joint venture agreement alone, in the absence of other evidence to show any trading activity on the part of the appellant, does not make the venture an adventure within the ambit of s. 2 of the Act.

The respondent cited *Leeming v. Jones (supra)* where the following conditions were considered in order to determine whether the appellant's activities amounted to an adventure or concern in the nature of trade –

a. The existence of an organisation;

b. Activities which lead to the maturing of the asset to be sold;

c. The existence of special skill, opportunities in connection with the article dealt with; and

d. The fact that the nature of the asset itself should lend itself to commercial transactions.

We are of the considered view that none of the badges of trade and/or conditions enumerated above is applicable in the case of the appellant.

The *Malaysian Taxation - Principles and Practice*, 5th edn by Choong Kwai Fatt says at p. 168 –

> 7.0 Badges of trade
>
> Over the years, the courts in Malaysia have laid down various guidelines or tests to distinguish gains arising from the disposal of an investment and gains from trade or an adventure or concern in the nature of trade. There are 10 badges of trade and **it is the total effect of all relevant factors and circumstances that determine the substance of the transaction**.
>
> It is interesting to note that on one hand the tax authorities would use the 'badges of trade' to argue that taxpayer is 'adventure in the nature of trade' and thus any profit will be assessable as business income. On the other hand, the taxpayer is relying on the same 'badges of trade' and holding the view that he is merely realising a long-term investment, which is of capital in nature. Any gains would be capital receipts. The test is the same but the perspective of each party is entirely different. It rests with the learned Special Commissioners and judges of the court to decide on the issues in dispute.
>
> (Emphasis is ours.)

The subject land was acquired by inheritance and not purchased for purpose of resale at a profit. The appellant's late father Yong Nam held the land since 1954 – more than 40 years at time of disposal. The appellant did not have any organisation and had not entered into any transactions in land, he did not do any alteration or change the character or quality or carry out any activity to render the land more saleable and no special exertion was made to find or attract purchasers by opening an office or advertising extensively.

The mere fact that an agreement was entered into or that the subject land was disposed of for a relatively high price does not make the transaction a trade or an adventure in the nature of trade.

The fact that the appellant worked as a marketing executive in the oil industry before his retirement does not amount to satisfying the third criteria in *Leeming v. Jones (supra)*, *ie*, existence of special skill, opportunities in connection with the article dealt with. The article dealt with here is land and not petroleum products.

The respondent cited what Viscount Dilhorne said in *I Investments Ltd (supra)*. It is not applicable in this case. The appellant here is not a company and the "individual" did not set himself up as a trader, did not declare his intention of trading and the transaction did not fall within the scope of his trade.

In fact, the appellant did not have any form of trade apart from being a retiree.

> Sir Nicolas Brown – Wilkinson V-C in the case of *Overseas Containers (Finance) Ltd. v. Stoker (HMIT)* [1989] BTC 153 in the Court of Appeal said that the commercial character of a transaction is normally determined objectively by the nature of the transaction itself i.e. is it a transaction of a kind similar to transactions of the same nature in the commercial world and carried out in a similar way (*IR Commrs v. Livingston* [1926] 11 TC 538 per Lord Clyde at p. 542). However, in addition to such outward badges of trade, the transaction must have a commercial purpose. If there was a genuine commercial purpose, the presence of a collateral purpose to obtain a tax advantage did not 'denature' what was essentially a commercial transaction. However, if the sole purpose of the transaction was to obtain a fiscal advantage, it was logically impossible to postulate the existence of any commercial purpose.
>
> (British Tax Reporter - Para 631-100)

We fail to understand the rationale of the respondent in this case.

In the absence of any of the accepted badges of trade or any other evidence which point towards trade or an adventure or concern in the nature of trade, it would be going against the policy adopted by the respondent as well as the decisions made by the special commissioners in cases of this nature hitherto.

The respondent had issued a Director-General's Circular No. 2 of 1986 dated 9 April 1986 on Real Property Gains Tax to provide some notes of guidance on issues and problems which have arisen or been encountered in the course of administering the Real Property Gains Tax Act 1976.

Paragraph 23 of the said Circular reads as follows –

> 23. Joint Venture with the developer
>
> There are instances of landowners entering into joint venture agreements with developers whereby the land landowner surrenders his land to the developer for development into a housing project and in return will be given a certain number of houses upon the completion of the project or alternatively paid a certain percentage of the proceeds (progress payments) from the sale of the houses built under the project.
>
> The facts of each cave must be duly examined to determine whether the profits arising from the joint venture are chargeable to income tax in the first place. **If there is insufficient evidence to show that the joint venture was a**

transaction in their carrying on of a trade or the transaction was an adventure in the nature of trade, the transaction will come within the scope of the Real Property Gains Tax Act.

The date of disposal will be the date of the joint-venture agreement. The consideration for the land is not the houses as they are not in existence or the portion of the sales proceeds as they are merely notional at the date of disposal, but the rights to own the houses upon completion of the project or receive a percentage of the sale proceeds when the project is on. The rights constitute an asset which the landowner receives in exchange for his properly. Since these rights do not have a market value at the time of disposal, being the date of signing the agreement, the market value of the land may be taken as the consideration for the disposal pursuant to the proviso to paragraph 13.

(Emphasis is ours.)

It is clear from the above that in the absence of sufficient evidence to establish trade or an adventure or concern in the nature of trade the whole transaction will come within the scope of the Real Property Gains Tax Act.

Had the appellant received the RM22,184,992 in cash in exchange for the land, the whole transaction would be chargeable to Real Property Gains Tax. This was agreed to by the respondent's counsel. Why then should it be classified as income chargeable under s. 4 (a) of the Act just by reason of the fact that the land was exchanged for units of the building constructed thereon to the same value in the absence of any evidence of trade or an adventure or concern in the nature of trade.

In this respect, *Whiteman on Income Tax (supra)* says at pp. 177 and 178 –

Clearly the problem whether the acts of a particular taxpayer do, or do not, amount to trading is often not an easy one; in borderline cases it is a question of degree, and the decision of the Commissioners, whichever way it goes, is unlikely to be disturbed. Probably the best approach to the problem in any given case is first to examine the taxpayer's acts and operations objectively to see whether they can fairly be called trading within the various decisions already discussed – or, to use Lord Buckmaster's phrase, "do they disclose an operation of business in carrying out a scheme of profit making?" If the answer to this question is in the affirmative, then a second question should be posed: "If it is not trading, what is it?" Is there some satisfactory explanation, consistent with the facts as found, which shows that the *prima facie* inference of trading was wrong? Clearly if the facts proved to the Commissioners satisfy them that the purpose of the operations was to provide the taxpayer with something for personal use, or a satisfactory investment, or some other benefit outside the ambit of trading, then the finding will be "no trade." But if no satisfactory explanation is forthcoming a finding of trading will then follow. An appellant who has been unable to convince the Commissioners that he has not engaged in an adventure in the nature of trade on any other basis may

well be compelled to rely on the following dictum of Donovan L.J. (as he then was) in delivering judgment in 1961 in *Jenkinson v. Freedland*:

> It cannot be right, therefore, to assert, as the Crown did before us, that whenever something is bought to resell at a profit an adventure or concern in the nature of trade necessarily results, and any finding of the Commissioners to the contrary must be perverse. Otherwise there would hardly be any need to introduce a capital gains tax. lt would virtually be here already. The true position, in my opinion, is that all the facts in each case must be considered, not merely the motive of acquisition, and a conclusion arrived at from such a comprehensive review.

Perusal of the joint venture agreement between the appellant and Lot One (p. 12 of exh. C) reveals the following –

a. The appellant is neither a shareholder nor a director of Lot One (cl. 3.2);

b. The appellant was not entitled to any share in the profits or be liable for the losses, if any. On the contrary he shall be indemnified against all losses, damages and costs (cl. 6.2);

c. Upon approval of the development order, even before the construction takes place, the units were valued and appropriated in accordance with the 18 - 82% basis between the appellant and the developers;

d. Clause 5.2 provides for the appellant to be kept informed of the monthly meetings and a quarterly progress report on the status of the project;

e. Clause 5.5 states that Lot One shall at its own cost and expenses construct and complete the project; and

f. Clause 5.9 provide for liquidated damages to be paid to the appellant in the event of Lot One failing to complete the construction within the specified period;

Based on the above as well as on other terms in the joint venture agreement, it is abundantly clear that it was not a joint venture business within the meaning of the Act.

The fact that the appellant reserved a right to have the planning and building plans discussed with and reviewed by him prior to the submission to the approving authority was merely to monitor the progress of the project in his pursuit to ensure that he was not short changed as he was in the joint venture with Sunrise Sdn. Bhd. prior to the joint venture with Lot One. Further, though Lot One paid the RM1 million to Sunrise Sdn. Bhd., it was at the expense of the appellant who incurred a loss on the percentage of the units due to him, from 20% to 18%.

Therefore, it is our considered view that the participation of the appellant in the meetings of Lot One, offers made by him to assist in the sales, monitoring and supervising the performance of the terms of the joint venture agreement, all put together, without more, do not make it a trade or an adventure or concern in the nature of trade as contended by the respondent.

The respondent cited the cases of *L v. CGIR (supra)* and *Martin v. Lowry (supra)*. We are of the view that both these cases do not apply in the case before us because they both can be distinguished and are decisions based on the facts of those cases.

In *L v. CGIR*, the appellant ('L') –

- formed a syndicate with the object of erecting houses;
- the land was re-zoned on his application;
- the land was valued and the amount of the value was regarded as his contribution to the syndicate; and
- the syndicate would pay the valued sum as well as one-half of the nett profits of the venture at the end of the development.

Hence the High Court set aside the special commissioners' decision and held that the transaction was an adventure in the nature of trade.

In *Martin v. Lowry*, the appellant ('Martin') –

- purchased vast supply of linen;
- embarked on an extensive advertising campaign, rented offices and engaged an advertising manager, a linen expert as adviser and a staff of clerks;
- account books normally kept by a trader were kept; and
- all receipts and payments in connection with the linen were passed through separate banking account.

The commissioners for the special purposes of the Income Tax Acts, the King's Bench Division, the Court of Appeal and the House of Lords all held that the transactions constituted the carrying on of a trade in view of the factors enumerated above.

Hence, we rejected the applicability of the principles in the two cases above to the case before us.

In the light of the foregoing, we are more than satisfied that the appellant has discharged his onus of proving that the assessment against which the appeal is made is excessive or erroneous successfully in respect of issue No. 1.

As regards issue No. 2, we did not make an order in view of our finding that the gains from the disposal of the subject land in issue No. 1 are not subject to income tax. Therefore, the year of assessment is irrelevant.

Accordingly, we, unanimously, allowed the appeal and discharged the respondent's assessment to which the appeal relates.

The material part of the deciding order dated 31 January 2000 that we made is in the following terms –

> **Rayuan Ini** setelah dibicarakan pada 24 Januari 2000 dengan kehadiran Encik S. Somaskantham dibantu oleh Encik Jayatharan a/l Thamotharam Pillai, Agen Cukai, bagi pihak Perayu dan Puan Hazlina binti Hussain, Pegawai Undang-Undang dan Puan Kanaga Devi a/p Shanmugam, Pegawai Penaksir, Lembaga Hasil Dalam Negeri bagi pihak Responden
>
> **Adalah Diputuskan** bahawa keuntungan daripada pelupusan hartanah EMR 5103 Lot No. 1, Mukim Kuala Lumpur bukanlah pendapatan yang boleh dikenakan cukai di bawah seksyen 4(a) Akta Cukai Pendapatan 1967
>
> **Maka Dengan Ini Adalah Diperintahkan** bahawa rayuan ini dibenarkan
>
> **Dan Diperintahkan Selanjutnya** bahawa Notis Taksiran Tambahan No. OG 0253 126-07 bertarikh 8 Disember 1998 yang menunjukkan RM7,579,027.74 sebagai cukai yang kena bayar bagi Tahun Taksiran 1992 dilepaskan.

The respondent being dissatisfied with our decision, has, by a Notice of Appeal dated 18 February 2000, required us to state a case for the opinion of the High Court pursuant to para. 34 sch. 5 of the Act, which case we have stated and do sign accordingly.

The question for the opinion of the High Court is whether, on the facts as stated by us, our decision is correct in law.